FILED
DEC 30 1941
CHARLES ELMORE CROPLEY
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 821

THOMAS D. AIKEN, TILLIE DAVENPORT, LILLIAN H. ESSIG, PAUL FETCHENEROWSKI, ELLA A. GALLAGHER, JOHN WILLIAM HAM, E. MORTON INGRAHAM, ADA L. JAMES, JUNEA W. KELLY, PETER J. McARRON, JOHN W. OSBORN, AUGUST H. PETERSON, VICTOR A. RASMUSSEN, GUS H. TESSMAN, C. J. UNGS, JEFFERSON D. WALTERS, JOHN P. YOUNG, FRANK S. PIPER, CHARLES P. BECKER AND BERTHA D. WILLIAMS,

Plaintiffs-Petitioners,

vs.

SAMUEL INSULL, JR., PHILIP J. McENROE, JOHN F. GILCHRIST, EDWARD J. DOYLE, JOHN G. GULICK, GEORGE F. MITCHELL, MARSHALL E. SAMPSELL, STUYVESANT PEABODY AND HARRY L. STUART,

Defendants-Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

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INDEX.

PAGE

Petition for Writ of Certiorari 1
Statement of the Matters Involved 1
Jurisdiction of This Court to Review the Decree in Question 7
The Questions Presented 7
Reasons for the Allowance of the Writ 9
Brief in Support of Petition for Writ of Certiorari .. 17
Opinions of the Courts Below 17
Jurisdiction 18
Statement of the Case 18
Specifications of Errors 19
Argument 20
I. Under Illinois Law the So-Called Settlement by the Debenture Holders With the Pledgee-Banks Coupled With the Reservation of the Cause of Action by the Debenture Holders Against the Defendants Did Not Operate to Release the Defendants 20
II. By Virtue of the Fact That the Suits Against the New York Banks Had Resulted in Judgment for the Banks at the Time of the So-Called Settlement With the Banks, the Debenture Holders Had No Cause of Action Against the New York Banks at the Time of the So-Called Settlement and Hence, to the Extent of the Pledges to the New York Banks, There Was No Basis for Invocation of the Alleged Rule That the Release of the Cause of Action Against One Joint Tort-Feasor Releases the Entire Cause of Action 31

III. The Defendants and the Pledgee-Banks Were Not Joint Tort-Feasors in Connection With the Pledging of the Assets of I. U. I. and Consequently There Was No Basis for the Application of the Alleged Rule That the Release of One Joint Tort-Feasor Releases All..... 33

Conclusion 35

CASES CITED.

Adams Express Co. v. Beckwith, 100 Ohio St. 348, 126 N. E. 300 25
Albert v. Sullivan, 287 Ill. App. 461, 465-7 12
Arkansas National Bank v. Martin, 110 Ark. 578, 163 S. W. 795 (1914) 14
Barnes v. Barnett, 188 Ill. App. 32 14
Belden v. Burke, 25 N. Y. Supp. 601 13
Benjamin v. McConnell, et al., 4 Gilman 536 22
Black v. Martin, 88 Mont. 256, 292 Pac 577 25
Bland v. Lawyer-Cuff Co., 72 Okla. 128, 178 Pac. 885 (1919) 25
Boyd v. Schneider, 131 Fed. 223 (C. C. A. 7) 13
Carey v. Bilby (C. C. A. 8), 129 Fed. 203 25
Carpenter v. W. H. McElwain Company, 78 N. H. 118, 120, 97 A. 560, 561 25
Chapin v. Chicago & E. I. R. Co., 18 Ill. App. 47 33
Chase Nat. Bank v. Sweezy, 281 N. Y. S. 487 14
Chicago Title & Trust Company v. Munday, 297 Ill. 555, 562 12
City of Chicago v. Babcock, 143 Ill. 358, 367 ... 11, 12, 22, 23
City of Topeka v. Brooks, 99 Kan. 643, 164 Pac. 285 .. 25
Clark v. Mallory, 83 Ill. App. 488, aff'd 185 Ill. 227 ... . 11, 23, 24, 29
Colby v. Walker, 86 N. H. 568, 171 Atl. 774 25
Connecticut Company v. New York, N. H. and H. R. Co., 94 Conn. 13, 107 Atl. 646 14
Davis v. Virginia Ry. & Power Co., 229 Fed. 633 (C. C. A. 4) 13

Delano v. Case, 121 Ill. 247 12

Dougherty v. Calif. Kettleman Oil R. Inc., 13 Calif. (2) 174 15

Dougherty v. California Kettleman Oil Royalties, 13 Calif. (2) 174, 88 P. (2d) 690 (1939) 14

Duck v. Mayeu, 2 Law Rep. Queen's Bench Div. 511, 513 25

Dupee v. Blake, 148 Ill. 453, 465 ..... 11, 22

Dwy v. Connecticut, 89 Conn. 74, 92 Atl. 883 25

Edens v. Fletcher, 79 Kans. 139, 98 Pac. 784 25

El Paso & S. R. Co. v. Darr, 93 S. W. 166 25

Feighley v. C. Hoffman & Son Milling Co., 100 Kan. 430, 165 Pac. 276 25

Flannery v. Flannery Bolt Co., 108 Fed. (2) 531, (C. C. A. 3, 1940) cert. denied, 60 S. Ct. 615 14

Forster v. Sheridan Trust & Savings Bank, 257 Ill. App. 463, 472 ..... 11, 22

Gilbert v. Finch, 173 N. Y. 455, 66 N. E. 133 ..... 25, 28

Greenhalch v. Shell Oil Co., 78 F. (2d) 942 (C. C. A. 10) 25

Jackson v. Ludeling, 88 U. S. 616 13

Skinner v. Sullivan, 127 Ill. App. 657, 663 ..... 11, 23

Kelly v. Hanover Bank & Trust Co., 11 Fed. Supp. 497, 85 Fed. (2d) 61 13

Kropidlowski v. Pfister & Vogel Leather Co., 149 Wis. 421, 135 N. W. 839 25

LaMonte v. Lurich, (N. J.) 100 Atl. 1031 25

Lumberman's Ins. Co. v. Preble, 50 Ill. 332, 335 ..... 11, 22

Lynch v. Conger, 168 N. Y. Supp. 855, 858, affirmed 229 N. Y. 543 13

Mahaffey v. Glover, 184 Ark. 1159, 45 S. W. (2d) 521 .. 25

Miller v. Lloyd, 181 Ill. App. 230, 246.....11, 22
Moore v. Stanwood, 98 Ill. 605, 608.....11, 22, 24
Mueller v. Dobschuetz, 89 Ill. 176.....11, 22
Nickerson v. Suplee, 174 Ill. App. 136, 139.....11, 23
Nixon v. City of Chicago, 212 Ill. App. 365, 387.....11, 22
Parmelee v. Lawrence, 44 Ill. 405.....11, 12, 21, 22
Pennington v. Bevering, 9 S. W. (2d) 401..... 25
Petroyeanis v. Pirola, 205 Ill. App. 310..... 29
People v. Becker, 253 Ill. 131.....15, 34
Pittsburgh Rys. Co. v. Chapman, 145 Fed. 886 (C. C. A. 3) 15
Rice v. Barkman, 249 Ill. App. 127, 130.....11, 22
Rice v. Webster, 18 Ill. 331..... 22
Roseville Trust Co. v. Mott, 85 N. J. Eq. 297, 96 Atl. 402 25
Scharfenstein v. Forest City Knitting Co., 253 Ill. App. 190, 202 (certiorari denied by Illinois Supreme Court, 254 Ill. App. xviii).....14, 35
Stanley v. Leahy, 87 Ill. App. 465..... 28
Strauss v. United States Fidelity & Guaranty Co., 63 Fed. (2) 174, 179 (C. C. A. 4)..... 13
Thomason v. Clark, 31 Ill. App. 404, 407.....11, 23
Van Meter v. Gurney, 251 Ill. App. 184, 186.....
.....11, 12, 22, 29, 32
Van Meter v. Gurney, 251 Ill. App. 184..... 15
Veazie v. Williams, 49 U. S. 134.....14, 34
Wallace v. Armstrong, 236 Ill. App. 457, 460.....11, 22
Wells v. Carlsen, 130 Neb. 773, 266 N. W. 618..... 13
Whitford v. Moehlenpah, 196 Wis. 10..... 13
Young v. Anderson, 33 Idaho 522..... 15

MISCELLANEOUS.

25 California Law Review 413 (1937)..... 26
13 Cornell Law Quarterly 473 (1928)..... 26
22 Minnesota Law Review 692 (1938)..... 26
Mich. Section 1 (Suppl. Mich. L. Rev.) 23 (1935)..... 26
34 Harvard Law Review 442 (1921)..... 26
The Restatement of Torts (1939), Sec. 885.....12, 26, 31

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Defendants-Respondents.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Statement of the Matters Involved.

This is a class suit in equity filed February 3, 1933 by holders of debentures issued by Insull Utility Investments, Inc. (called herein for convenience "I.U.I."), against the

directors of I.U.I. principally on two causes of action: (1) for inducing and causing the pledging of substantially all the corporation's assets to certain banks in violation of covenants in the debentures held by the plaintiffs, and (2) for liability under an Illinois statute for declaring or assenting to dividends in impairment of capital or while insolvent (R. 2-38).

In respect to the second cause of action, relating to liability for improper dividends, the Court of Appeals reversed the decree of the District Court which had sustained defendants' motion to dismiss for failure to state a cause of action, the Court of Appeals holding that the complaint states a cause of action and that the District Court should have permitted the plaintiffs to file certain tendered amendments to the complaint (R. 357-363, 364). This second cause of action, therefore, is not involved in this petition for certiorari.

The cause of action involved in this petition for certiorari is that relating to the liability of the directors for inducing and causing the pledging of the assets of I.U.I. to certain banks in violation of the debenture covenants. In respect to that cause of action, the District Court entered a decree (R. 320) on March 8, 1940 sustaining a motion by defendants for summary judgment under Rule 56 of the Rules of Civil Procedure predicated on the alleged ground that by a so-called settlement of separate litigation by the debenture holders against the pledgee-banks, in which litigation the debenture holders sought to establish equitable rights in the pledged assets, the debenture holders, in effect, released the bank pledgees and that such release operated to release the directors (defendants here) of all liability in connection with their having induced such pledges (R. 74). The Court of Appeals affirmed the decree in that respect (R. 352-357, 364) and it is to that portion of the decree that this petition for writ of certiorari is addressed.

The Essential Facts.

I.U.I. was organized as an investment company in the latter part of 1928 by Samuel Insull (since deceased) and the defendants, who became its directors (R. 3-5). The publicly stated purpose of I.U.I. was to acquire and hold large share-holdings in the major utility companies of the Insull group, which were also under the direction and management of the defendants and in which they had large financial interests (R. 3-5). The defendants caused I.U.I. to issue and sell to the public shortly after its organization two series of long term unsecured debentures, aggregating $66,000,000, in denominations of $1,000 each (R. 6, 12, 16). The debentures contained certain covenants for the benefit and protection of the debenture holders, the one of principal importance here being as follows:

> "The Company hereby covenants and agrees with the holder hereof that so long as this debenture shall be outstanding and provision for the payment thereof shall not have been made, it will not mortgage or pledge any of its property unless the instrument creating such mortgage or pledge shall provide that this debenture shall be secured thereby equally and ratable with all other obligations issued or to be issued thereunder, * * *." (R. 8, 14.)

These debentures were purchased by the public, including plaintiffs, in reliance upon representations made by the defendants in public reports and offering circulars, representing the nature and purpose of the company and the relationship of the defendant-directors to the other Insull companies whose securities were to be acquired and held as aforesaid, and the further representations that the holders of debentures would be protected by said covenant and that the proceeds of the financing would enable I.U.I. to pay all existing indebtedness and leave a substantial cash balance, about $19,500,000 (R. 4, 5, 16-19, 106, 256-262).

Shortly after I.U.I. was organized, the defendant-directors caused I.U.I. to pledge substantially all its assets (securities of the Insull group) to secure loans from various banks in Chicago and New York and General Electric Co. aggregating $75,000,000 (R. 24-32) of which about $45,000,000 remained unpaid when I.U.I. went into bankruptcy in 1932, at which time its unpledged assets consisted only of some $1,700,000 of securities and cash (R. 96, par. 18). Inasmuch as none of the pledges to the banks provided for the equal and ratable security of the debentures, the defendant-directors, in causing said pledges to be made, induced the violation of the debenture covenants (R. 24-33).

After I.U.I. went into bankruptcy, the debenture holders filed two sets of suits, one against the banks and the other is this suit. These suits were filed in behalf of owners of over $57,000,000 of outstanding debentures (R. 6, 12). The suits against the banks charged that the banks had knowledge of the debenture covenants at the time they received the assets of I.U.I. in pledge and the relief sought was a decree requiring the banks to share their security with the debenture holders as required by the covenant (R. 86-114, 124). The suits against the New York banks were tried in the District Court at New York and resulted in decrees of dismissal. (*Celia Kelly* v. *Central Hanover Bank & Trust Co., et al.*, 11 F. Supp. 497.) That court found, among other things (page 510), that the banks were charged neither with fraud nor with inducing the breach of covenant. On appeal these cases were remanded by the Circuit Court of Appeals for the Second Circuit for further findings of facts (85 F. (2d) 61, as modified by Order of July 17, 1936 (R. 121, 463).

Negotiations were thereupon entered into as a result of which both the New York and Chicago litigation against the banks was terminated, in consideration, among other things, of a sum equal to 10% of the then value of the collateral to be paid by the banks into the District Court at Chi-

cago for the benefit of the debenture holders, which amounted to $3,435,088.07 (R. 136-138, 232-238). It was distinctly intended and agreed by the banks and the representatives of the debenture holders that this cause of action against the directors of I.U.I. should not be released or affected by the so-called settlement with the banks (R. 235-238), and the settlement agreement was made subject to the approval of the District Court at Chicago after notice to debenture holders of all its terms and a public hearing (R. 238-239, 143, 144, 148-162). This so-called settlement agreement did not take the form of an instrument of release but was embodied in a petition by the debenture holders to the District Court at Chicago, the answer of the Chicago banks and the findings of facts, conclusions of law, decree and orders entered by said court (R. 115-199) which approved the settlement as fair and equitable on the terms and conditions therein set forth (R. 170, 171, 173), one of the terms being that the cause of action of the debenture holders against the directors would not be released or affected by the settlement. This reservation clause reads as follows (R. 143, 166):

> K. Nothing in the agreement of settlement and compromise contained, or referred to therein, to be construed to operate as a release or to affect any causes of action, claims or demands held by the said complainants in said Chicago and New York equity suits or by said Bigelow as Trustee, or by the holders of said Insull Utility Investments, Inc., Series A or B Debentures, or any other creditors of said Insull Utility Investments, Inc., against any person, firm or corporation other than any party to the settlement and compromise by name or reference and any officer, director, agent or employee of such party who is not or has not also been an officer or director of said Insull Utility Investments, Inc.

The various findings and orders in connection with the approval of said settlement were entered by District Judge

Wilkerson before whom the instant case was then and had been pending for several years (R. 56-65).

After the so-called settlement with the banks was consummated, the directors (defendants here) filed their above-described motion for summary judgment under Rule 56 of the Rules of Civil Procedure, attaching thereto copies of said papers filed in connection with the approval of the bank settlement, which included said reservation clause, and claimed thereby that the settlement with the banks operated to release the directors (R. 74-195). The plaintiffs filed an answer (R. 229-241), the allegations of which were admitted by defendants (R. 279, 281, 289), in which it was alleged that the reservation clause was inserted in the settlement papers with the banks for the reason that it was the purpose and intention of the plaintiffs and the banks not to release the directors and that the agreement with the banks was no more than a covenant not to sue. The plaintiffs' answer further alleged that the payment by the banks and all the dividends paid to the debenture holders by the bankrupt estate of I.U.I. yielded less than 10% of the principal amount of debentures and that the payment by the banks to the debenture holders did not constitute nor was it paid or received as full satisfaction of the injuries sustained by the debenture holders as the result of the bank pledges in violation of the debenture covenants (R. 238-240).

The District Court sustained the defendants' motion for summary judgment (R. 320) and this was affirmed by the Court of Appeals (R. 364). In its opinion (R. 352) the Court of Appeals recognized that under the Illinois rule in contract cases the release of one joint obligor, coupled with a reservation of the cause of action against the other joint obligors, does not operate to release the other obligors, but the Court said that "strange though it may seem, the Illinois courts have not seen fit to extend this wholesome and common sense formula to the tort cases." The Court

of Appeals stated that the "superior view" is that the other joint tort-feasors are not released but felt that the "harsh" and "technical" rule (that words of release override and are paramount to other words used by the parties expressing the contrary intention not to release and to regard the entire transaction as no more than a covenant not to sue) was followed in Illinois in tort cases and must be applied by it (R. 355-357).

The plaintiffs filed a petition for rehearing in the Court of Appeals on the ground that the Court of Appeals misapprehended the Illinois law, that no case in Illinois has refused to extend the wholesome and common sense formula used in contract cases to tort cases and that in no case have the Illinois courts decided that the release of one joint tort-feasor, coupled with an express reservation of the cause of action against the other tort-feasors, constitutes a release of the other tort-feasors (R. 365). This petition for rehearing was denied without opinion (R. 461).

Jurisdiction of This Court to Review the Decree in Question.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, c. 229 (28 U. S. C. A. Section 347). The decree which the petitioners seek to have reviewed was entered by the Circuit Court of Appeals of the Seventh Circuit, on August 22, 1941 (R. 364). The opinion is reported in 122 F. (2d) 746 and appears in the record (R. 352). Petitions for rehearing were denied October 1, 1941 (R. 461).

The Questions Presented.

1. Inasmuch as the so-called settlement with the banks, which was made in Illinois, expressly reserved the cause of action by the debenture holders against the defendants,

should not the Court of Appeals have held that the defendants were not released in view of the Illinois rule that a release of one jointly liable, with a reservation of the cause of action against the others jointly liable, does not release the others?

2. In the absence of a decision by the state courts on the question of local law as to the effect of a reservation clause in a release of joint tort-feasors, should not the Circuit Court of Appeals, in view of decisions by the state courts giving effect to reservation clauses in releases of joint contractual liability, have applied the local law, especially when the Circuit Court of Appeals recognized that the local rule applied in those cases was common sense and wholesome and saw no reason for any distinction in the application of the rule to all releases with such express reservations, whether the liability was in contract or in tort?

3. In the absence of decisions by the state courts on a question of local law, should not the Circuit Court of Appeals have followed the rule adopted in other states and the Restatement of the Law of Torts and which it recognizes as a wholesome and common sense rule rather than the rule which it considered "harsh" and "technical" and which ignores the intention of the parties?

4. Were the banks by the acceptance of the assets in pledge with knowledge of the violation of the debenture covenants, but without any fraud and without inducing the breach of the covenants, liable as tort-feasors or were they merely liable in equity to account to the debenture holders for their equal and ratable security in the pledged assets?

5. By inducing I.U.I. to breach the covenants in favor of the plaintiffs by pledging substantially all of the assets of I.U.I. to the banks in violation of the debenture covenants, were the defendants liable as ordinary tort-feasors,

or in view of the nature of the company and the circumstances under which the debentures were sold, were they liable as trustees? Should the defendants, as trustees in the situation disclosed by this suit, be entitled to avail themselves of the alleged rule that the release of one joint tort-feasor releases all?

6. Is it true that the defendant-directors and the Chicago and New York bank-pledgees were *jointly* liable for the same wrong so that there could be invoked the alleged rule that the release of one joint tort-feasor releases the others?

7. Inasmuch as the cause of action of the debenture holders against the New York banks had been extinguished by judgments having been entered for the banks in the suits brought against them by the debenture holders and the debenture holders could do no more than appeal from such judgments, the plaintiffs, at the time of their so-called settlement with the banks, had no cause of action against the New York banks. In view of the fact that the debenture holders had no cause of action against the New York banks and could and did agree to do no more than dismiss their pending appeals, did the Court of Appeals properly invoke the alleged rule in respect to the cause of action for wrongful pledges to the New York banks?

8. Should the District Court have considered this matter, over the objections of the plaintiffs, on a motion for summary judgment under Rule 56 of the Rules of Civil Procedure despite the fact that the plaintiffs had demanded a jury trial on questions triable by a jury and the intention of the parties was an important factual issue? (See R. 239, 264, 279-281, 289.)

9. Should the plaintiffs be barred from prosecuting their cause of action against the defendants when it is clear that whatever payments the plaintiffs have received from the Chicago and New York banks and all other

sources do not satisfy the cause of action by the plaintiffs against the defendants and constitute payment of less than ten per centum of the principal amount of the debentures? Should the debenture holders be precluded from maintaining this suit against the defendant-directors when the amount of money which they received from the Chicago and New York banks did not compensate them in full for their damages nor was it accepted as full compensation?

10. The holding of the Court of Appeals vitiates the acts of the District Court in connection with the approval of the settlement and deprives the debenture holders of the benefit of the reservation, which was a condition precedent to the settlement and an inducement to them to consent and to the District Court to approve the settlement as fair and equitable. The Court of Appeals should have given effect to the reservation, leaving the defendants to benefit from the settlement only to the extent that it reduces the amount of damages for which they are liable, as was intended by the settling parties, including the District Court.

Reasons for the Allowance of the Writ.

1. The Court of Appeals has decided an extremely important question of local law in conflict with applicable local decisions. In construing releases the Illinois courts follow the cardinal rule of construction that written instruments must be so construed as to carry out the intention of the parties. Since 1867, all Illinois cases involving the question have without exception decided that whenever a release, even though using words of release as to the releasee, also contains language manifesting an intent to preserve the releasor's rights against others jointly liable, such manifestation must be given effect and this is done by treating the release as if it were only a covenant not

to sue the releasee, leaving the cause of action against the others unimpaired:

Parmelee v. *Lawrence,* 44 Ill. 405.
City of Chicago v. *Babcock,* 143 Ill. 358, 367.
Dupee v. *Blake,* 148 Ill. 453, 465.
Moore v. *Stanwood,* 98 Ill. 605, 608.
Mueller v. *Dobschuetz,* 89 Ill. 176.
Lumberman's Ins. Co. v. *Preble,* 50 Ill. 332, 335.
Forster v. *Sheridan Trust & Savings Bank,* 257 Ill. App. 463, 472.
Van Meter v. *Gurney,* 251 Ill. App. 184, 186.
Rice v. *Barkman,* 249 Ill. App. 127, 130.
Wallace v. *Armstrong,* 236 Ill. App. 457, 460.
Nixon v. *City of Chicago,* 212 Ill. App. 365, 387.
Miller v. *Lloyd,* 181 Ill. App. 230, 246.
Nickerson v. *Suplee,* 174 Ill. App. 136, 139.
Skinner v. *Sullivan,* 127 Ill. App. 657, 663.
Clark v. *Mallory,* 83 Ill. App. 488, aff'd 185 Ill. 227.
Thomason v. *Clark,* 31 Ill. App. 404, 407.

The Court of Appeals recognized that this is the Illinois rule in contract cases, but stated that "strange though it may seem, the Illinois courts have not seen fit to extend this wholesome and common sense formula to tort cases", and added that it failed "to see a good reason for drawing this distinction between joint tort-feasor cases and joint debtor cases * * * but we must accept the limitation fixed by the Illinois courts." The Circuit Court of Appeals cited no case to support such a limitation, relying only on three cases which involve the effect of a release of joint tort-feasors where there was no expressed intention to reserve the cause of action against others. In our petition for rehearing filed in the Court of Appeals we challenged defendants to cite a single case in Illinois supporting the distinction made by the Court of Appeals and deciding that in spite of a clause in a release preserving

the cause of action against the other joint tort-feasors, the reservation clause will be given no effect and the other joint tort-feasors will be released. The defendants answered the petition for rehearing but were unable to cite a single case to meet this challenge.

2. Even assuming that the Illinois courts have not decided the question as to whether the release of one joint tort-feasor, with a reservation against the other tort-feasors, does or does not operate to release the other joint tort-feasors, and that therefore it was necessary for the Circuit Court of Appeals to fill the gap, the Court of Appeals should have filled the supposed gap by applying the rule followed in Illinois in contract cases which it found to be analogous and which it recognized as the "superior view" and the "wholesome and common sense formula" (and which is also the prevailing rule in tort cases followed by the other state courts and adopted by the Restatement of the Law of Torts) rather than the supposed rule that in tort cases in Illinois such reservations are disregarded, which the Court of Appeals admitted was "harsh" and "technical."

If the point here involved were presented to the Illinois courts, they would unquestionably hold that the rule in *Parmelee* v. *Lawrence*, 44 Ill. 405, applied to tort cases. This is indicated in *City* v. *Babcock*, 143 Ill. 358, and *Van Meter* v. *Gurney*, 251 Ill. App. 184, both of which involve tort liabilities.

3. The Court of Appeals has decided an important question of local law, namely, that the defendants are not liable as trustees to the debenture holders but as ordinary tort-feasors, which decision is in conflict with applicable local decisions:

Delano v. *Case*, 121 Ill. 247.

Chicago Title & Trust Company v. *Munday*, 297 Ill. 555, 562.

Albers v. *Sullivan*, 287 Ill. App. 461, 465-7.

The decision of the Court of Appeals on this point is also in conflict with the decisions of this Court, other Circuit Courts of Appeal and other state courts:

Jackson v. *Ludeling*, 88 U. S. 616.
Boyd v. *Schneider*, 131 Fed. 223 (C. C. A. 7).
Strauss v. *United States Fidelity & Guaranty Co.*, 63 Fed. (2) 174, 179 (C. C. A. 4).
Davis v. *Virginia Ry. & Power Co.*, 229 Fed. 633 (C. C. A. 4).
Whitford v. *Moehlenpah*, 196 Wis. 10.
Lynch v. *Conger*, 168 N. Y. Supp. 855, 858, affirmed 229 N. Y. 543.
Belden v. *Burke*, 25 N. Y. Supp. 601.
Wells v. *Carlsen*, 130 Neb. 773, 266 N. W. 618.

4. The decision of the Court of Appeals that the bank pledgees were tort-feasors in accepting the pledges from I.U.I. is in direct conflict with the findings of the District Court in the litigation against the banks concerning the same pledges here involved (*Kelly* v. *Central Hanover Bank & Trust Co.*, 11 Fed. Supp. 497) and of the Circuit Court of Appeals on review thereof (85 Fed. (2d) 61), as modified (R. 463).

Judge Mack in his opinion, in describing the suits against the banks, found (pp. 500, 510):

> "Plaintiff asks, on behalf of herself and all other debenture holders and for their benefit, that stock pledged to defendants by I.U.I. as collateral to certain loans made by each of them in 1931, be returned or that the debenture holders share equally and ratably with those defendants in such securities. * * * defendants are charged neither with actual fraud nor with inducing a breach of contract."

The Circuit Court of Appeals for the Second Circuit said, in describing the suits against the bank, stated (p. 62):

> "A debenture bondholder, Kelly, brought a representative suit against all the lenders jointly and against

each bank individually, praying that the pledgees be ordered to surrender the property pledged and that she be decreed to have a superior lien on such pledged property."

It therefore appears that the liability of the banks, if any, which was the subject of the settlement was *ex contractu*, involving only an obligation to share the securities as required by the debenture covenants, and not in tort. Cases in Illinois and in other jurisdictions demonstrate that the liability of the banks, if any, was of a contractual nature and not in tort and that a release of one liable in contract does not discharge the liability of the other who was liable in tort, even though his wrongful act initiated the transaction:

Barnes v. *Barnett*, 188 Ill. App. 32.

Dougherty v. *California Kettleman Oil Royalties*, 13 Calif. (2) 174, 88 P. (2d) 690 (1939).

Flannery v. *Flannery Bolt Co.*, 108 Fed. (2) 531, (C. C. A. 3, 1940) cert. denied, 60 S. Ct. 615.

Arkansas National Bank v. *Martin*, 110 Ark. 578, 163 S. W. 795 (1914).

See: *Connecticut Company* v. *New York, N. H. and H. R. Co.*, 94 Conn. 13, 107 Atl. 646; and *Chase Nat. Bank* v. *Sweezy*, 281 N. Y. S. 487.

5. The decision of the Circuit Court of Appeals that the defendant-directors and the banks were *jointly* liable as tort-feasors is in conflict with the local law and the decisions of this Court and other courts that even though the acts of two parties contribute to an injury, they will not be deemed joint tort-feasors under the technical rule of release in the event that their liability arises from different grounds and on different theories:

Veazie v. *Williams*, 8 How. (U. S.) 134.

Scharfenstein v. *Forest City Knitting Co.*, 253 Ill. App. 190, 202 (certiorari denied by Illinois Supreme Court, 254 Ill. App. xviii).

People v. *Becker*, 253 Ill. 131.
Dougherty v. *Calif. Kettleman Oil R. Inc.*, 13 Calif. (2) 174.
Young v. *Anderson*, 33 Idaho 522.
Pittsburgh Rys. Co. v. *Chapman*, 145 Fed. 886 (C. C. A. 3).

6. The decision of the Court of Appeals decided an important question of local law, namely, that the debenture holders released their cause of action against the defendants for the wrongful pledges to the New York banks at the time when they entered into the so-called settlement with the New York banks even though, at that time, the debenture holders had no cause of action whatsoever against the New York banks because of the judgments entered in the bank suits in favor of the New York banks. This decision is in direct conflict with the local decisions (*Van Meter* v. *Gurney*, 251 Ill. App. 184).

7. It would be in the interest of the proper administration of justice to grant a writ of certiorari in this suit in order to correct a plainly untenable and erroneous decision based on undisputed facts. The so-called settlement between the debenture holders and the banks was consummated under the supervision and with the approval of the District Court at Chicago having jurisdiction of the bankruptcy case of I.U.I., the suits against the banks and this suit. The decision of the Court of Appeals frustrates and negatives the decree approving the so-called settlement with the banks, which decree was entered on the express condition that the cause of action against the defendants would be reserved for the benefit of the thousands of debenture holders scattered throughout the country.

The questions presented by this petition are of great public importance both in this suit and to correct the Court of Appeals' conception of the Illinois law on a principle of

law which is applicable to situations which arise with great frequency.

WHEREFORE, your petitioner prays that the Writ of Certiorari be issued under the seal of this Court directed to the United States Circuit Court of Appeals, for the Seventh Circuit, commanding that Court to certify and send to this Court on a day to be designated, a full and complete transcript of the record and of all proceedings in the Circuit Court of Appeals had in this cause to the end that this cause, insofar as it involves the summary judgment barring the plaintiffs from maintaining the cause of action against directors for having induced the wrongful pledging of assets, may be reviewed and determined by this Court; that the judgment of the Circuit Court of Appeals affirming said summary judgment be reversed; and that the decree of the District Court insofar as it allows said summary judgment be set aside; and that your petitioners be granted such other and further relief as may be proper.

Respectfully submitted,

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